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FISCAL IMPACT STATEMENT

LS 6494

BILL NUMBER: HB 1292

NOTE PREPARED: Jan 3, 2003

BILL AMENDED:

SUBJECT: Local Property Tax Replacement Income Tax.

FIRST AUTHOR: Rep. Kruse

FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: ☒ GENERAL
☒ DEDICATED
☐ FEDERAL

IMPACT: State & Local

Summary of Legislation: The bill allows a county council to impose a Property Tax Replacement Income Tax (PRIT) not exceeding 1% for the county and to use tax revenues for property tax replacement credit. The bill provides a state distribution to local units in an adopting county in the amount of 20% of the PRIT imposed by the county. The bill allows the additional distribution to be used for local road and street funding.

Effective Date: Upon passage; July 1, 2003.

Explanation of State Expenditures: See *Explanation of Local Revenues* for a detailed explanation of the bill and the impact to the state Property Tax Replacement Fund.

Administrative Impacts: Under the bill, the Department of State Revenue (DOR) would have additional cost for the administration, audit, and collection of taxes. The State Budget Agency would be required to determine the annual certified distributions of the Property Tax Replacement Income Tax (PRIT) revenues for all adopting counties. The Department of Local Government Finance would determine the distribution of county PRIT revenues to all the civil taxing units within the adopting county. These responsibilities may require additional resources depending on how many counties would choose to adopt PRIT and at what rate. The state agencies listed above all receive state General Fund money for their operating expenditures.

Explanation of State Revenues:

Explanation of Local Expenditures:

Explanation of Local Revenues: *General Overview:* This bill establishes a new local option income tax that

could be used to replace property taxes for local units with the exception of schools and solid waste management districts. The tax would be on individual adjusted gross income of county residents and non-residents working in the county who do not pay a similar tax in their county of residence. The tax may be imposed, increased, and reduced in increments of 0.1%. The maximum tax rate for county residents is 1%. The non-resident rate is limited to 0.3% and could never exceed the resident tax rate. The PRIT tax may be adopted and adjusted independently of all other local income taxes (CAGIT, COIT, CEDIT). No maximum combined rate would exist between PRIT and other local income taxes that are assessed by a county. Revenues collected from PRIT may be used to replace property taxes or to increase the homestead credit against property tax liability for resident homeowners.

1. PRIT for Property Tax Replacement: PRIT revenues, under this bill, may be distributed, budgeted, and used in the same manner as property taxes. If all counties adopted PRIT at the full 1%, revenues would be approximately \$1.165 B in CY 2004 and \$1.224 B in CY 2005. The estimates were generated based on the forecast growth rates in individual income tax revenue from the December 18, 2002, revenue forecast. The forecast growth rate is 3.8% over FY 2003 and 5.1% over FY 2004.

The amount of PRIT collected and used to replace local property taxes would impact distributions from the state Property Tax Replacement Fund. The state pays Property Tax Replacement Credits (PTRC) in the amount of 60% of school general fund levies attributable to all property and 20% of the portion of all operating levies (including the remaining 40% of the school GF levy) that are attributable to real property and non-business personal property. The state also pays homestead credit in the amount of 20% of the net property tax due on owner-occupied residences. As PRIT revenues increase, the county's gross property tax liability will decrease and with it, the PTRC and homestead credit funds received from the state.

In order to compensate PRIT counties for the reductions in their PTRC and homestead credit, the bill requires the state to make a contribution to the adopting counties equal to 20% of PRIT revenues used to replace property taxes. In theory, counties with a mix of PRIT and property taxes would receive the same amount of state support as they do currently, but it would be a mix of PTRC, homestead credit, and the additional distribution. However, due to certain exceptions the non-school PTRC rate is less than the full 20%. In CY 2004, the total amount of non-school PTRC is about 10% of the total non-school levy, including levies for cumulative and debt funds. ($[100\% \text{ levy} - 50\% \text{ non-qualifying levies}] * 20\% = 10\%$). As a result, adopting counties would actually receive slightly more money from the state than those counties that did not adopt PRIT.

There are several differences between PTRC / homestead credit and the additional distribution under PRIT. First, PTRC and homestead credit replace and therefore reduce local property taxes. The state contribution equal to 20% of PRIT revenues does not replace any local taxes, but is additional revenue to the county. Second, the statutory use of these two state disbursements is different. PTRC and homestead credit, like property taxes, go directly into the operating budgets of the local units. The new revenue from the state equal to 20% of PRIT revenues must be used for local road and highway expenditures.

2. PRIT for Homestead Tax Credits: Under this bill, PRIT may also be used to increase the homestead tax credit. The homestead tax credit is a credit against the property tax liability of resident homeowners. Most of the credit is provided by the state. The other is provided by counties that have adopted a county option income tax (COIT). Counties may currently increase the 20% state rate by a maximum of 8%. The bill provides no limitations on how much the credit may be increased using PRIT.

Projected Impacts: The exact impact of PRIT would depend on whether it is used to:

- 1) replace property taxes collected for the civil units within the county,
- 2) increase the homestead credit for county resident homeowners, or
- 3) do both simultaneously.

The impact would also depend on the PRIT rate that is adopted by the county and how much of the county's property taxes are replaced. Three scenarios are provided to illustrate the possible impacts of this bill. They are as follows:

These scenarios are examples, and are to be used only for illustrative purposes.

1. PRIT is used to replace property taxes: For this example, assume that a county's gross property tax levy is \$1 M. Under the current law, approximately 10% of this levy would be paid by the state as PTRC and 8% would be paid by the state as homestead credit, leaving 82% to be paid by property tax revenues (see explanation above). If PRIT is used to replace \$500,000 of the property taxes, the gross property tax levy will be only \$500,000. The PTRC and homestead credit would be reduced because they would be based on a \$500,000 levy rather than the full \$1M levy. Together, revenues will equal 50% PRIT, 5% PTRC, 4% homestead credit, and 41% property taxes. In addition, the county would also receive the additional state distribution equal to 20% of the PRIT that is used for property tax replacement. The following table shows this impact:

Revenue Sources	Before PRIT		With PRIT	
Property Taxes	\$820,000	82%	\$410,000	41%
State Property Tax Replacement Credits	100,000	10%*	50,000	5%
Homestead Credit	80,000	8%*	40,000	4%
PRIT used for property tax replacement			500,000	50%
TOTAL	1,000,000	100%	1,000,000	100%
State Additional Distribution (20% of PRIT)			100,000	Add
TOTAL	1,000,000		1,100,000	110%
<p>* PTRC is equal to 20% of non-school operating levies except those attributable to business personal property. The total amount of non-school PTRC is about 10% of the total non-school levy, including levies for cumulative and debt funds : ([100% levy - 50% non-qualifying levies] * 20% = 10%).</p> <p>** Homestead credit is equal to 20% of the net (after PTRC) tax due on owner-occupied homes. Homesteads account for about 44% of the tax base. Homestead credit as a percent of all levies is about 8% of the total: (90% net levy [after PTRC] * 44% homesteads * 20% credit = 8%).</p>				

Therefore, under scenario one, the county would collect \$100,000 more in revenue under the bill than under the current law which would be used for local road and highway expenditures. The state would also distribute more funds to an adopting county than under current law (\$190,000 versus \$180,000).

Under this scenario, property taxpayers in the county will pay lower property taxes. The current homestead

credit percentage would stay the same. Income earners may experience an overall increase in tax liability if their income exceeds the value of their property. Businesses would benefit from a reduction in their property taxes and would not be subject to PRIT.

2. All of PRIT is used to increase the homestead tax credit: If all the revenue collected through PRIT is used to increase the homestead tax credit to homeowners, county revenues would remain the same. The county would not receive the additional state distribution on PRIT since none of the revenues were used to replace property taxes. The sole beneficiary of this scenario would be the county homeowners who would receive more homestead credits and thus pay less in property taxes.

3. PRIT funds are used for both property tax replacement and the homestead credit: PRIT may also be used for both property tax replacement and the homestead credit. Under this scenario, the county would receive the additional state funding equal to 20% of the PRIT used to replace property taxes. Overall, the state's contribution to the county would increase slightly as discussed above. For example, instead of \$500,000 of PRIT used for property tax replacement, only \$400,000 is used, with the other \$100,000 used for homestead credit. The additional state distribution would be 20% of the \$400,000 only, or \$80,000. All of the county's property taxpayers would realize a reduction in their tax liability from the PRIT property tax replacement. Homeowners would accrue additional benefits from the increase in the homestead credit.

State Agencies Affected: Department of State Revenue, Department of Local Government Finance, State Budget Agency, Auditor of the State, Treasurer of the State.

Local Agencies Affected: Adopting counties.

Information Sources: State Budget Agency, *December 18, 2002, State Revenue Forecast*.

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